

BRIEF SUMMARY OF THE CONFERENCE AGREEMENT ON H.R. 4242
(The Economic Recovery Tax Act of 1981)

A. INDIVIDUAL INCOME TAX REDUCTIONS

1. Rate reductions.--Cumulative across-the-board rate reductions of 23 percent by 1984: 1.25 percent for 1981 with cumulative reductions of 10 percent for 1982, and 19 percent for 1983, and 23 percent for 1984.
2. Top rate.-- Reduces the top marginal rate on investment income from 70 percent to 50 percent, effective January 1, 1982.
3. Capital gains.--The highest capital gains tax rate is reduced to 20 percent for sales or exchanges occurring after June 9, 1981.
4. Deduction for two-earner couples.--Provides additional tax relief to two-earner married couples in the form of a deduction of 5 percent of the earnings of the lesser earning spouse (up to \$1,500) in 1982 and a 10-percent deduction (up to \$3,000) in 1983 and thereafter.
5. Indexing.--Individual rate brackets, the personal exemption, and the zero bracket amount will be adjusted for inflation starting in 1985.
6. Foreign earned income.--Starting in 1982, Americans working abroad will be entitled to an exclusion of \$75,000 as well as a housing allowance. The exclusion increases to \$95,000, by \$5,000 increments, by 1986.
7. Above-the-line charitable deductions.--Nonitemizing taxpayers will be able to take a deduction for charitable contributions. The deduction is equal to a percentage of contributions (with a fixed dollar limit for 1982-1984), as follows:

| | | |
|-----------------------|-----------|------|
| 25 percent (to \$100) | | 1982 |
| 25 percent (to \$100) | | 1983 |
| 25 percent (to \$300) | | 1984 |
| 50 percent | | 1985 |
| 100 percent | | 1986 |

B. GENERAL BUSINESS PRODUCTIVITY PROVISIONS

1. Capital cost recovery.--Starting January 1, 1981, the cost of 10-year, 5-year, and 3-year classes of property may be recovered by using rates that approximate the 150-percent declining-balance method through 1984. (Certain long-lived utility property will be in a 15-year class.)

For property placed in service in 1985, and 1986 and thereafter, recovery rates will be increased to 175 percent and 200 percent, respectively. Property in the 3-year class will get a 6-percent investment tax credit and property in the 5-, 10-, and 15-year classes a 10-percent credit.

Starting in 1982, taxpayers can elect to expense \$5,000 annually, increasing in stages to \$10,000 in 1986.

2. Real estate.--Real estate will have a 15-year, audit-proof, cost recovery period and will be written off using rates equivalent to 175-percent declining-balance (low-income housing, 200-percent declining balance).
3. Leasing.--The conference agreement provides a liberalized leasing rule to help transfer the capital cost tax benefits to companies which can utilize them.

C. SMALL BUSINESSES

1. Corporate tax rates.--Reduces the tax rate on taxable income below \$50,000 in two steps to 15 percent on the first \$25,000 of income and 18 percent on the next \$25,000 by 1983.
2. Investment credit.--Increases the investment credit limit for used property from \$100,000 to \$125,000 for 1981-84 and thereafter to \$150,000.
3. Subchapter S.--Increases the maximum number of Subchapter S shareholders to 25. In some circumstances, trusts also will be permitted to be shareholders.

4. Accumulated earnings credit.--Increases from \$150,000 to \$250,000 the minimum accumulated earnings credit.
5. Inventory accounting.--Simplifies inventory accounting for businesses with average gross receipts of less than \$2 million.

D. RESEARCH AND EXPERIMENTATION

1. Incremental credit.--Provides a 25-percent income tax credit for post-June 1981 R&E expenditures.
2. Equipment contributions.--Provides a liberalized rule for certain corporate contributions of new R&E equipment.
3. R&E allocations.--Allocates all U.S. R&E expenditures to U.S. source income for the next two years.

E. OTHER BUSINESS PROVISIONS

1. Stock options.--Allows employees favorable tax treatment on certain stock options.
2. Rehabilitation expenditures.--Allows a 15 percent credit for rehabilitation expenditures for 30 year old buildings, a 20 percent credit for 40 year old buildings, and a 25 percent credit for certified historic buildings.

F. SAVINGS INCENTIVES

1. Savings certificates.--Individuals may exclude from income, on a one-time basis, up to \$1,000 (\$2,000 on joint returns) of interest paid on depository institution tax-exempt savings certificates issued after September 30, 1981 and before January 1, 1983.
2. Individual retirement accounts.--The maximum contribution to an individual retirement account (IRA) is increased from \$1,500 to \$2,000, up to 100 percent of an individual's earnings for the year. The maximum contribution to a spousal IRA is increased from \$1,750 to \$2,250. Both of these changes are effective January 1, 1982.

3. Employer plans.--Individuals who are active participants in an employer-sponsored retirement plan will be able to deduct up to \$2,000 per year of voluntary contributions to individual retirement accounts, effective January 1, 1982.
4. Keogh plans.--The maximum deductible contribution to a Keogh plan is increased from \$7,500 to \$15,000, effective January 1, 1982.
5. ESOPs.--Allows a tax credit based on payroll for contributions to an ESOP. For 1983 and 1984, the percentage will be 0.5 percent; from 1985 through 1987 the credit will be 0.75 percent.
6. Dividend reinvestment.--Individual shareholders in a domestic public utility may exclude up to \$750 (\$1,500 on a joint return) from income if received as a common stock dividend.
7. Net interest exclusion.--Starting in 1985, there will be a 15-percent net interest exclusion.

G. ESTATE AND GIFT TAX REDUCTIONS

1. Credit.--Increases the unified credit as follows:

| <u>Year of death</u> | <u>Amount of credit</u> | <u>Equivalent amount</u> |
|----------------------|-------------------------|--------------------------|
| 1982 | \$ 62,800 | \$225,000 |
| 1983 | 79,300 | 275,000 |
| 1984 | 96,300 | 325,000 |
| 1985 | 121,800 | 400,000 |
| 1986 | 155,800 | 500,000 |
| 1987 and thereafter | 192,800 | 600,000 |

2. Tax rates.--The maximum estate and gift tax rates are reduced from 70-percent to 50-percent over a four-year period. (The reduction is five-percentage points per year.)
3. Marital deduction.--Starting in 1982, there will be no limit on the marital deduction and the gifts and bequests of life estates will qualify for the deduction in certain cases.
4. Gift tax exclusion.--Increases the annual gift tax exclusion from \$3,000 to \$10,000, effective in 1982.

5. Special use valuation.--Simplifies and liberalizes the special use valuation provision.
6. Tax payments.--Simplifies and liberalizes the deferred tax payment provisions.

H. ENERGY PROVISIONS: WINDFALL PROFIT TAX

1. Royalty owners.--Allows a \$2,500 credit for 1981, and an exemption for 2 barrels in 1982-1984, and for 3 barrels thereafter.
2. Newly discovered oil.--Reduces the tax rate from 30 to 15 percent between 1982 and 1986.
3. Stripper oil.--Starting in 1983, exempts stripper oil of independent producers.
4. Charities.--Exempts residential child care homes.

I. OTHER ITEMS

1. Substantially reduces the ability to use tax straddles.
2. Modifies numerous tax administrative and penalty provisions.
3. Extends the fringe benefit moratorium until 1984.
4. Extends the targeted job credit through 1982.
5. Provides a permanent rule for State legislators, retroactive to the beginning of 1976.
6. Increases the deduction limit for corporate charitable contributions from 5 to 10 percent.
7. Allows a deduction for certain adoption expenses.
8. Provides special rules for reorganization of financially troubled thrift institutions.
9. Provides special rules for mutual savings banks that convert to stock associations.
10. Increases the deductible amount for gifts and awards made to employees.
11. Increases the bad debt deduction reserve for commercial banks for 1982.
12. Modifies the payout rule for private foundations after 1981.
13. Provides technical amendments to the tax on the sale of U.S. real property to foreign investors.

14. Extends permanently the exemption of low-income housing from the section 189 rule for amortization of construction period taxes and interest.
15. Increases the amount of qualified low-income housing rehabilitation expenditures eligible for 5-year amortization.
16. Extends for two years (through 1984) the 1-percent telephone excise tax.
17. Modifies the tax treatment on gain on the disposition of stock in a foreign investment company.
18. Provides tax exemption for certain bonds issued by volunteer fire departments.
19. Provides tax exemption for certain industrial development bonds used for the purchase of mass transit equipment.
20. Provides that political organization taxable income of a congressional candidate's campaign fund is taxed at the generally applicable corporate income tax rates.
21. Modifies the railroad retirement tax provisions.
22. Increases the estimated tax payment requirement for large corporations, phased in over a 3-year period.
23. Increases the minimum threshold amount for declaration and payment of estimated taxes by individuals, over a 4-year period.
24. A one-year FUTA tax exemption for certain fishing boat crew members currently exempt for purposes of FICA and income tax withholding.
25. Provides, with certain limitations, a 7-percent maximum rate of imputed interest under section 483.

Summary of Estimated Revenue Effects of the Provisions of
H.R. 4242 as Approved by the Conference, Fiscal Years 1981-86
(Millions of Dollars)

| Provision | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 |
|----------------------------------|---------------|----------------|----------------|-----------------|-----------------|-----------------|
| Individual income tax provisions | -39 | -26,929 | -71,098 | -114,684 | -148,237 | -196,143 |
| Business tax cut provisions | -1,562 | -10,657 | -18,599 | -28,275 | -39,269 | -54,468 |
| Energy tax provisions | -- | -1,320 | -1,742 | -2,242 | -2,837 | -3,619 |
| Savings incentive provisions | -- | -263 | -1,821 | -4,215 | -5,740 | -8,375 |
| Estate and gift tax provisions | -- | -204 | -2,114 | -3,218 | -4,248 | -5,568 |
| Tax straddles | 37 | 623 | 327 | 273 | 249 | 229 |
| Administrative provisions | -- | 1,182 | 2,048 | 1,856 | 718 | 592 |
| Miscellaneous provisions | -1 | -88 | 267 | 561 | 61 | -275 |
| TOTAL REVENUE EFFECT | -1,565 | -37,656 | -92,732 | -149,944 | -199,303 | -267,627 |

